Responsible Investment

Corporate Governance and SRI – Q1 2005

Contents

*A Mellon Financial Company*SM

NEWTON
The Power of Ideas

Voting profile for Q1 2005

The first quarter of a year tends to be a quiet period for General Meetings. Q1 2005 did not prove to be an exception. Newton voted on behalf of its clients at 223 separate company meetings in the first quarter of 2005. UK companies accounted for 141 of these meetings. Newton voted against one or more resolutions at almost 8.5% of all meetings held within the quarter. Some companies, predominantly in the Asia-Pacific region, continue to put a voting resolution to shareholders seeking approval of "Other Business". Most companies expect few, if any, issues to arise under this item. However, Newton routinely votes against the approval of "Other Business" due to the unknown nature of its possible contents.

The following charts provide a summary of voting during Q1 2005. Overseas, Newton took no action at eight AGMs and five EGMs. This reflected the need, in these cases, to "block" the shares before exercising voting rights. Being unable to trade a shareholding for potentially long periods of time has obvious dangers.

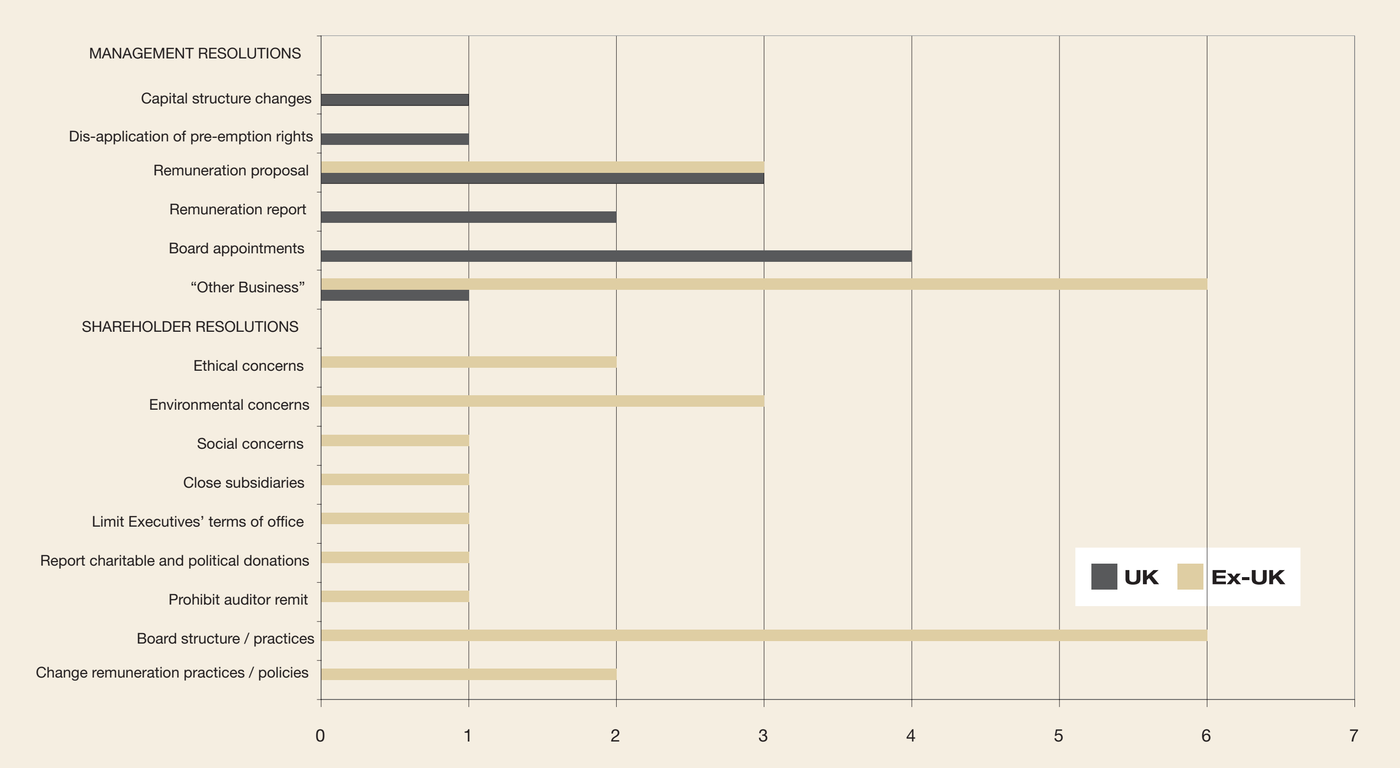
UK voting summary – Q1 2005

AGM	**88**
Voted in favour of all resolutions	82
Voted against one or more resolutions	5
Took no action	1
Abstained	0
EGM	**49**
Voted in favour of all resolutions	48
Voted against one or more resolutions	1
Took no action	0
Abstained	0
SGM	**0**
Voted in favour of all resolutions	0
Voted against one or more resolutions	0
Took no action	0
Abstained	0
Court Meeting	**4**
Voted in favour of all resolutions	4
Voted against one or more resolutions	0
Took no action	0
Abstained	0
TOTAL	**141**
Voted In Favour	**134**
Voted against	**6**
Took no action	**1**
Abstained	**0**

Overseas voting summary – Q1 2005

AGM	**60**
Voted in favour of all resolutions	40
Voted against one or more resolutions	12
Took no action	8
Abstained	0
EGM	**22**
Voted in favour of all resolutions	16
Voted against one or more resolutions	1
Took no action	5
Abstained	0
SGM	**0**
Voted in favour of all resolutions	0
Voted against one or more resolutions	0
Took no action	0
Abstained	0
Court Meeting	**0**
Voted in favour of all resolutions	0
Voted against one or more resolutions	0
Took no action	0
Abstained	0
TOTAL	**82**
Voted In Favour	**56**
Voted against	**13**
Took no action	**13**
Abstained	**0**

Breakdown of resolutions voted against during Q1 2005



UK Companies

Aberdeen Asset Management – EGM – 24/03/2005
Following the expiry of the company's 1994 Long-Term Incentive Plan (LTIP), a resolution was proposed to shareholders seeking approval for the adoption of a new LTIP. Newton voted against the resolution due to the rules of the LTIP containing special provisions in the event of a change in control, which contravene best practice in this area.

Barclays Investment Funds (Channel Islands) – Sterling Bond – AGM – 08/03/2005
A single resolution seeking to re-elect collectively six retiring directors was voted against. Newton was concerned over the bundling of what should have been separate resolutions for the re-election of retiring directors. Also, Newton felt that it was not appropriate to appoint a non-executive director to the audit committee, who was affiliated to the company.

A further resolution, entitled "Other Business", was voted against. This resolution could provide for decisions being taken that may not be in the best interest of shareholders. Additionally, Newton would not have adequate time to properly assess items raised under this resolution.

First Choice Holidays – AGM – 10/03/2005
Newton is fundamentally against retrospective changes to long-term incentive awards. To this end, a vote against was cast in relation to two resolutions seeking approval of a significant change to performance conditions that govern the vesting of existing share option and restricted share awards. The company admitted that the change would result in an absolute increase in the value of awards. This, coupled with the fact that the base year for assessing the new performance conditions would be calculated from a low performance year, 31st October 2003, meant that Newton could not support the two resolutions.

Grainger Trust – AGM – 24/02/2005
Several areas of the remuneration policy and composition of the remuneration committee caused concern. Of the three members of the remuneration committee, one had recently retired from the company's property valuers, one was a partner at the company's auditors and the other is a trustee of an estate that controls 10% of the company's share capital. The operation of the company's restricted share plan provides for a high level of vesting for achieving median performance and no financial underpin exists to support the Total Shareholder Return performance measure. In addition, two executive directors have service contracts that provide for two years' notice. Newton felt that the structure of the remuneration committee and its policy were not appropriate. Votes were cast against the remuneration report and two members of the remuneration committee, who were seeking re-election to the board.

JP Morgan Fleming Asian Investment Trust – AGM – 04/02/2005
Two resolutions were voted against. These were in relation to the sale of ordinary shares held in the company's treasury account. If passed, the resolution would allow the company to re-issue shares at a discount to their Net Asset Value and not necessarily on a pre-emptive basis to existing shareholders. Given existing shareholders could be negatively impacted through this method of issuing treasury shares, Newton felt that it could not support the resolutions.

Majedie Investments PLC – AGM – 19/01/2005
Newton voted against the resolution seeking approval of the remuneration report and also against a non-executive director, who was seeking re-election to the remuneration committee.

The company failed to provide details of maximum potential awards under its annual bonus and share option scheme. Also, performance conditions governing the vesting of option grants may be re-tested throughout the life of the award. Newton felt that the company's rationale for retaining re-testing provisions was not appropriate. The company explained that the impact of management decisions may have a longer time horizon than companies in other sectors and that to have fixed length performance periods would likely lead to increased volatility. Newton would have preferred that the company address this issue by way of an extension to the performance period of share option awards to, for example, five years from three years.

Ex-UK Companies

Advanced Info Service – AGM – 30/03/2005
A resolution entitled "Other Business" was voted against. This is a routine resolution in Thailand. However, it potentially allows companies to raise and pass issues of concern on the day of the meeting without giving shareholders adequate time to assess the underlying details.

Airports of Thailand Public Co Ltd – AGM – 31/05/2005
A vote against was instructed for a resolution entitled "Other Business". Shareholders would not be made aware of the content of the resolution until the day of the meeting. This would not provide adequate time for shareholders to assess any underlying detail in order to make an informed decision.

Asahi Glass Co Ltd – AGM – 30/03/2005
Newton voted against a resolution seeking approval of a new executive share option plan. The intended recipients of the proposed share options include "related companies" and non-executive directors. The company failed to specify who the "related companies" were or at what level they would expect to award the share options. There were also no details of the proposed awards to non-executive directors. Given the perceived conflicts of interest arising from such a distribution of share options, Newton felt that it could not support the resolution.

In addition, Newton also voted against a resolution requesting approval of retirement bonuses to statutory auditors and special payments to continuing statutory auditors. The company had designated one of the retiring auditors and both of the continuing auditors as independent internal auditors. Newton felt that the payment of discretionary bonuses and special payments undermines the independence of designated independent statutory auditors.

Bank of Nova Scotia – AGM – 01/03/2005
A shareholder proposed a resolution requiring the company to close its operations in tax havens. The proponent argued that tax havens are used to evade tax and commit tax fraud, and encourage money laundering and criminal activity. The company generates 27% of its earnings from international operations and, within these jurisdictions, the company operates in compliance with national and international laws intended to detect and deter tax evasion, terrorist activity and organised crime. Additionally, the company does not operate in any of the areas identified by the OECD as uncooperative tax havens. Newton voted against the shareholder proposed resolution.

Votes against were cast in relation to shareholder proposed resolutions that sought to fix a maximum wage ceiling for senior employees and to replace share options with restricted share awards. Newton felt that imposing arbitrary limits on executives and dictating the method of awarding share incentives could prove problematic for the company in attracting, retaining and motivating senior employees. Although Canadian best practice on remuneration is not as advanced as it is in the UK, the company does operate a relatively modest and stringent policy versus its competitors. The remuneration committee also consists entirely of independent non-executive directors.

A further shareholder resolution requested the company to limit the tenure of non-executive directors to ten years. Newton voted against this resolution. It was felt that imposing such a limit would be too restrictive on the company. Newton prefers all members of the remuneration and audit committees to be independent. However, when evaluating corporate strategy, companies can enjoy the value of experience, at little cost, through the continued tenure of non-independent non-executive directors versus the cost of commissioning expensive consultants. The company has also shown a commitment to refreshing its board. Votes were instructed against this resolution.

Newton voted against a shareholder proposed resolution requesting the company to report on its efforts to reduce the risk impact of climate change. Newton perceives the company's disclosure on such matters as being ahead of some of its key competitors but there are areas where improvement would be appropriate. Having said this, the company has yet to make public its 2004 accountability statement. The company has made considerable progress over the past two years in relation to its environmental risk management systems and reporting. The company has also adopted the Equator principles, which provide it with a comprehensive framework for the continuing development and improvement of related risk management systems, monitoring and reporting. Newton also expects the company to improve in this area given that Canadian government policy for Kyoto implementation is being taken to the next level in the near future.

The company currently adopts a strategy of reviewing the appropriateness of keeping non-executive directors on its board when they change their main occupation. Newton voted against a shareholder resolution that requested immediate resignation of non-executive directors if they change their main occupations.

The final shareholder proposed resolution sought for the company to alter its credit card operating policy by placing the interests of cardholder clients ahead of the interests of merchants and others. The bank reaffirmed its commitment to all clients. As such, in the event of a dispute between clients, the bank strives to protect and balance interests of all the parties in the VISA credit card system, within the standardised rules of this system and the applicable laws. Newton voted against the shareholder proposed resolution.

East European Food – AGM – 15/02/2005
Newton voted against a resolution entitled "Other Business". Such requests are often routine in certain jurisdictions. However, giving blanket approval of unknown items may not be in shareholders' best interests.

Fortum Oyj – AGM – 31/03/2005
A shareholder resolution proposed at the company's AGM sought the abolition of its Supervisory Board and to replace it with a Unitary Board structure. There is little empirical evidence to suggest that either approach is superior to the other. Also, Finnish company law does not dictate the approach that companies should take. Therefore, Newton did not support the resolution.

A second shareholder resolution requested the company to abolish the existing nomination and remuneration committees and replace them with a single committee covering both nomination and remuneration. However, the resolution proposed that the constituents of this new committee should be representatives of three major shareholders and the company's chairman. Newton believes that it is not in shareholders' best interests to delegate such authority to individuals that do not have a fiduciary duty to shareholders. Also, the appointment of executive board members should receive a high level of input and be, in part, the responsibility of the CEO. Similarly, the chairman should be responsible and accountable for the appointment of non-executive directors. Newton voted against the shareholder proposed resolution.

KT Corp – AGM – 11/03/2005
A total of four candidates were proposed for election to three positions on the company's board. The method of cumulatively voting is common in South Korea where, in this case, the three directors with the greatest numbers of votes become elected to the board. Of the four candidates, one was a shareholder proposed nominee. However, this candidate had little relevant experience relative to the other candidates. Newton voted against the election of the shareholder proposed candidate.

Land & Houses Public Co Ltd – EGM – 27/01/2005
A resolution sought shareholder approval for "Other Business" that may be raised on the day of the company's AGM. Shareholders would not be given the opportunity to adequately assess any items raised under this resolution. Therefore, a vote against was instructed.

Lucent Technologies Inc – AGM – 16/02/2005
Newton voted against two resolutions proposed by shareholders at the company's AGM.

The company was asked to provide a detailed report, within five days of the meeting, relating to all direct and indirect political contributions and that this be made publicly available by way of publication in eleven US based newspapers. Newton did not support this proposal due to the company's compliance with all applicable reporting and public disclosure requirements surrounding political contributions. In addition, indirect contributions made by employees are not within the control of the company's management.

A further shareholder resolution requested a prohibition on the company's auditors from providing non-audit services. During 2004, Lucent was fined by the SEC and received a court ruling against it for financial improprieties. The company has now limited the services that may be performed by its independent auditors, which include audit related services and certain tax services. Newton felt it would be inappropriate to completely prohibit the company from allowing its auditor to take on certain tax services for the company. It is often the case that auditors are best placed to carry-out certain tax services. However, the company should be encouraged to give only limited non-audit and tax related work to its auditor and provide more detailed disclosure relating to the types and costs of services provided by all its accountants / consultants. To this end, Newton voted against the shareholder proposed resolution.

Monsanto Co – AGM – 20/01/2005
A shareholder resolution requested the company to establish a committee of independent directors to review and report to shareholders on policies and procedures used to monitor Genetically Engineered (GE) products. A majority of the company's revenues are generated from the production and sale of GE products. Therefore, the company faces unique risks and opportunities. The company is fully committed to co-operating with regulatory authorities and to the testing of its products. This may include gaining approval from the US Food and Drug Administration, US Environment Protection Agency and other regulatory bodies across the world. In addition to testing the viability of their own products and instigating research into GE production, the company addresses safety issues for its GE products and associated chemicals. This is published on its web site and in scientific journals. Given the lack of definitive evidence demonstrating any adverse effects of GE products and the company's responsible attitude, Newton voted against the shareholder resolution.

The company's level of disclosure, commitment to good practices and its compliance with relevant laws meant that Newton did not support a further shareholder resolution. This resolution requested the company to prepare a report identifying its pesticides that are considered, by the Environment Protection Agency, as "probable" or "likely" carcinogens.

A further shareholder filed a resolution asking the company to review and amend its code of business conduct to include a comprehensive human rights policy. Monsanto does operate and source products from countries with controversial human rights records. However, at the time of the shareholder proposition, the company was in the process of developing a formal code of conduct. Given this and the lack of controversy around Monsanto's human rights record, Newton did not support the shareholder resolution.

The final resolution, filed by a Monsanto shareholder, requested the company to eliminate the use of live animals when testing its products. The company has a responsible approach to the use of animals in the testing of its products. Animals are only used when required by regulations or to effectively ascertain information on the affect of products on employees, customers and the environment. Additionally, the company advocates non-animal testing methods when acceptable and further limits animal testing by sharing test data with other organisations. Newton voted against the shareholder proposed resolution.

Overseas-Chinese Banking Corp Ltd – AGM – 30/03/2005
Newton voted against a resolution entitled "Other Business". Such requests are often routine in certain jurisdictions. However, giving blanket approval of unknown items may not be in shareholders' best interests.

Siam Cement Co Ltd – AGM – 23/03/2005
A vote against was instructed regarding a resolution entitled "Other Business". This routine item would allow other issues, not contained in the company's official meeting agenda, to be raised and approved without providing shareholders with adequate time to assess the issues.

Varian Medical Systems Inc – AGM – 17/02/2005
Newton felt that it could not support the approval of the company's share option plan. The details of the plan did not specify the performance period or whether executive awards are subject to performance conditions. The plan would provide special provisions in the event of a change in control, whilst undermining the independence of non-executive directors by providing them with share option awards. Furthermore, it was felt that the potential dilution to existing shareholders of c.16% was excessive.

Examples of engagement – Corporate Governance

Whilst the first quarter of a year is relatively quiet in regards to companies holding General Meetings, it is fast becoming the time of year when companies consult their shareholders on proposed changes to remuneration policies. Newton believes that the forthcoming requirement for companies to expense share based incentive awards and the development of remuneration best practice were the two main drivers behind companies consulting their shareholders on remuneration matters during the first quarter of this year. Other than remuneration considerations, Newton also engaged with companies on corporate governance matters that included board appointments, board practices and succession planning.

Below are some examples of Newton's engagement with investee companies on corporate governance matters during the first quarter of this year.

UK Media and Entertainment Company – Jan 2005
Contact: Company Secretary

Newton was concerned at the company's continued use of its facility to re-test performance conditions that govern the vesting of awards made under the Executive Share Option Scheme (ESOS). Furthermore, Newton suggested that shareholders would take greater comfort in the company's restricted share plan if an additional performance condition to relative Total Shareholder Return governed the vesting of awards. The company stated that, following shareholders' concerns, it was reviewing the need to maintain the facility to re-test performance conditions under the ESOS. Newton expects that the facility to re-test performance conditions will be removed for future share option awards.

UK Support Services Company – Feb 2005
Contact: Executive Chairman

The company sought to make a minor adjustment to its share option plan. It was proposed that the exercise period of its long-term incentive plan be extended from seven years to ten years. Newton was supportive of the proposal but raised a concern relating to a statement, accompanying the consultation letter, that the company may increase the use of annual cash bonuses.

UK Utility Company – Feb 2005
Contacts: Chairman
Remuneration Consultant

The chairman of the company sought Newton's view on the continuation, for a further year, of one of the company's non-executive directors. The non-executive director was first appointed to the board in 1996. If appointed for a further year, he would not be deemed as independent due to his tenure exceeding nine years. Given the company had been going through significant changes of senior executive and non-executive board members, Newton were sympathetic with the need to maintain a level of continuity at a time when the company was in a transitionary period.

UK Real Estate Company – Feb 2005
Contacts: Chair of Remuneration Committee
Remuneration Consultant

A consultation paper was put to shareholders relating to proposed changes to the company's remuneration policy. Newton supported the company's intention to cease share option awards. Support was also given to the setting of challenging Earnings Per Share performance targets that would govern the vesting, in part, of the proposed deferred annual bonuses and restricted share awards. However, Newton's main concern related to the setting of Total Property Return (TPR) as a performance measure. Newton felt that TPR was a proper measure to use in assessing the company's performance. However, it was requested that the company provide additional detail on the setting of these targets given the proposal was to provide shareholders only with retrospective disclosure. The company stated that TPR would need to materially outperform the Weighted Average Cost of Capital (WACC) for awards to begin vesting and very significant outperformance would be required for maximum vesting of awards. It was also stated that awards would not vest if TPR was below the company's WACC.

UK Support Services Company – Mar 2005
Contact: Corporate Broker

The company's broker sought Newton's views on a proposal by the company to appoint its Chairman to the Audit Committee. The company stated that, over the past year, the Audit Committee had invited the company's Chairman to its meetings. It was unclear whether the Chairman had attended all meetings of the Audit Committee and what role he played when he was in attendance. Given that the Chairman was previously the CEO of the company, Newton felt that his involvement with the Audit Committee would be inappropriate unless his attendance was occasional and could be justified. Newton requested that in such a situation justification should be provided to shareholders within the company's annual report and accounts.

UK Transport Company – Mar 2005
Contacts: Chairman
Company Secretary

Newton's views were sought on the company's proposed changes to its remuneration arrangements. Newton was in agreement with the proposal to remove the Executive Share Option Scheme and increase the maximum annual bonus in line with the company's competitors. Furthermore, Newton was encouraged by the inclusion of safety targets as one of the contributing factors governing the award of annual bonuses. Of concern was the company's proposal to increase the CEO's base salary by c.28%. It was proposed that this would be applied historically so that the effective date of increase would be April 2004. The company did not provide any explanation for this methodology.

UK Transport Company – Mar 2005
Contacts: Chair of Remuneration Committee
Remuneration Consultant

The company proposed the removal of its Executive Share Option Scheme and introduction of a new Long-Term Incentive Plan (LTIP) and Deferred Annual Bonus (DAB). Newton queried the appropriateness of using a DAB for other executives given that award levels would not be disclosed and the matching of deferred shares would not be subject to the achievement of performance conditions. Under the proposals for senior executives, Newton were concerned that 50% of LTIP awards would only be subject to a relative Total Shareholder Return performance with no accompanying financial underpin. However, the remuneration committee would have to be satisfied that there had been an improvement in the underlying financial performance of the company. Newton sought assurances regarding the discretion to be used in assessing improvements in the underlying financial performance of the company. The company also proposed significant salary increases for two executive directors. Newton sought additional information that would demonstrate the company's policy of setting base salaries at a median level.

UK Oil & Gas Company – Mar 2005
Contacts: Director of Human Resources
Head of Investor Relations

The company held a series of meetings with investors to discuss its proposals to alter its remuneration policy. Broadly, the company was seeking to introduce performance targets that govern the award of matching shares under the deferred annual bonus arrangement, remove share options, increase restricted share awards and change the performance conditions governing the vesting of restricted share awards. Newton remained concerned that a quarter of matching shares, awarded under the deferred annual bonus, would not be subject to the achievement of performance conditions. It was also felt that the level of vesting for achieving median relative Total Shareholder Return performance was excessive for awards of restricted shares. Comfort was also sought regarding the level of discretion afforded to the remuneration committee. It was stated that the remuneration committee would use the company's unique scoring system to establish the achievement of underlying financial performance. However, this would not be applied as an exact science but indicative of achieved performance.

UK Pharmaceutical Company – Mar 2005
Contacts: Chairman
Company Secretary

A meeting was held with the company in order to gain a better understanding of its practices, policies and procedures relating to corporate governance matters. Given the company's relatively small market capitalisation and its dual listing on the London and New York Stock Exchanges, Newton was concerned over the pressures, risks and challenges that the company faces from a corporate governance perspective. Various matters were discussed including the enhancements to its Operating and Financial Review, board practices, board structure and its remuneration policy.

UK Aerospace & Defence Company – Mar 2005
Contact: Non-executive Director

The company sought Newton's view on a proposed candidate for appointment as the company's Chairman. Newton indicated its approval of the appointee and the succession process undertaken by the Nomination Committee. In particular, Newton considered that the proposed candidate's experience would benefit the company's performance. Newton was also encouraged that the appointee was independent from the company.

SRI Focus: Transparency in the Extractive Industries

Summary

The Extractive Industries[1] (EI) play an important role in economic growth and social development. Through the generation of revenues, creation of jobs, provision of basic raw materials necessary for the building of infrastructure and housing and for their contribution to technological developments, the EI are essential to meeting society's long-term and day-to-day needs.

Resource rich – economically poor

There has been a wide debate over the association between resource-rich countries and poor economic performance. There are many current examples of countries where oil, gas and mining operations are associated with poverty, conflict and corruption. This is especially true of the African continent. Long-term oil producers such as Nigeria, Angola, Cameroon and Gabon have been unable to convert their oil prosperity into broad-based economic wealth and poverty reduction. The discrepancy between the wealth generated by the EI and the lack of tangible benefits seen by local communities is often the basis for conflict in these regions. The primary responsibility for managing EI wealth in a transparent, fair and accountable way lies with governments. Making the flow of revenues between companies and governments transparent can help to generate accountability. It is then more likely that revenues will be used for country and community reform or development and less likely that revenues will be diverted into corrupt pockets.

The extent of this problem is wide and is not confined to Africa. Revenues from oil, mining and gas are critically important in about 60 developing or economic transition countries. Of the 3.5bn citizens in these countries, some 1.5bn live on less than US$2 per day. The World Bank identifies twelve of the world's most mineral-dependent states and six of the most oil-dependent states as Highly Indebted Poor Countries with among the worst Human Development Indicators in the world.

It is hoped that transparency, improved financial management and accountability will contribute to the better, more efficient and more equitable use of resources. This, in turn, should contribute towards an improved investment climate and a stronger economy while also creating a base for sustainable development.

Global drive to improve transparency

Significant progress has been made in this area. The G8 countries issued a Declaration on *Fighting Corruption and Improving Transparency* at Evian in 2003. In 2004, *Transparency Compacts* were agreed with four countries. The International Monetary Fund (IMF) promoted fiscal transparency in member countries via the *Code of Good Practices on Fiscal Transparency* and the associated manual. Implementation of the code is monitored through the production of *Reports on the Observance of Standards and Codes* (ROSCs). Both the IMF and the World Bank promote more effective resource revenue management through policy advice, policy-based lending, project lending and technical assistance. More recently, the Extractive Industries Transparency Initiative has entered its implementation phase.

The Extractive Industries Transparency Initiative (EITI)

The EITI is a voluntary initiative, launched at the World Summit on Sustainable Development, in Johannesburg, September 2002. The aim of the initiative is to encourage greater transparency and accountability in countries dependent on the revenues from oil, gas and mining.

Institutional investors have actively supported the EITI since it was launched. Newton, alongside a group of investors, representing £3.8 trillion of funds under management, issued a statement of support for the initiative.

EITI – Public disclosure

The EITI encourages Oil, Gas and Mining companies to publicly disclose all payments they make to developing country governments and for these governments to publish what they receive. Published information should be independently audited. The initiative is participative in nature and encourages governments, extractive industry companies, international agencies and Non Governmental Organisations (NGOs) to work together to develop a framework to promote transparency of payments from the EI. There is a clear role for civil society, which participates actively in the design, implementation and overview of the disclosure process. The objective of such wide participation is to create a country-owned process. In this way it is hoped that natural resource wealth, a cause of corruption and authoritarianism in many countries, can become key in the fight against corruption and authoritarianism, by giving leverage to those pushing for reform.

EITI – Progress

The initiative has made good progress since its launch in 2002, though implementation is still at an early stage with only Azerbaijan and the Kyrgyz Republic having actually published payment details. Eleven countries have now committed to implementing the initiative. This includes three new commitments made this quarter by the Governments of the Republic of Congo, Niger and Cameroon. Other governments that have made a commitment to the EITI include Timor Leste, Ghana, Nigeria, Peru, São Tomé e Príncipe and Trinidad & Tobago. However, it must be noted that transparency is only the beginning of a journey towards creating stable and functional environments. Improved governance, through the creation of policies on openness as well as checking and balancing procedures, is a major factor in creating a better operating environment, a level playing field where society and civilians gain the benefits from the wealth created by the extractive industries.

[1&2] The Extractive Industries (EI), for the purpose of this review, are defined as the Oil, Gas and Mining industries.

Country Focus: Nigeria

Nigeria is an example of a country where resource wealth has not transformed into economic success. Nigeria's economy is overwhelmingly dependent on the production of crude oil. Oil exports account for 96% of Nigeria's total exports. Political and ethnic strife has been disrupting oil production in Nigeria for nearly fifty years and disputes between oil companies, the government, and communities are common.

Company Focus: Shell

As institutional investors, and on behalf of our clients, Newton is mindful of the risks and responsibilities that companies face when they operate or have business relationships in troubled countries, such as Nigeria. Operating in this type of environment exposes companies to heightened business risks. As a significant investor in Shell Transport & Trading Plc, which is active in Nigeria, Newton felt it necessary to meet with the company's management to gain a better understanding and to seek assurance that the risks associated with operating in Nigeria are fully recognised and considered. In February 2005, Newton representatives met with four representatives from Shell to discuss these issues.

Conclusions drawn from the meeting were that Shell does face significant challenges in Nigeria but has experience in dealing with them. The company is aware of and understands the risks associated with operating in Nigeria. It also understands that it has a role to play in contributing towards the sustainable development of that society and that it can influence and encourage positive change.

Newton, on behalf of its clients, will continue to monitor Shell's operations and risk management procedures.

SRI Focus: Transparency in the Extractive industries

Full Report

Background

The Extractive Industries[2] (EI) play an important role in economic growth and social development. Through the generation of revenues, creation of jobs, provision of basic raw materials necessary for the building of infrastructure and housing, and for their contribution to technological developments, the EI are essential to meeting society's long-term and day-to-day needs.

There has been a wide debate over the association between resource-rich countries and poor economic performance. There are many current examples of countries where oil, gas and mining operations are associated with poverty, conflict and corruption. This is especially true of the African continent. Long-term oil producers such as Nigeria, Angola, Cameroon and Gabon have been unable to convert their oil prosperity into broad-based economic wealth and poverty reduction. The discrepancy between the wealth generated by the EI and the lack of tangible benefits seen by local communities is often the basis for conflict in these regions. The primary responsibility for managing EI wealth in a transparent, fair and accountable way lies with governments. Making the flow of revenues between companies and governments transparent can help to generate accountability. It is then more likely that revenues will be used for country and community reform or development and less likely that revenues will be diverted into corrupt pockets.

What is a resource-rich country?

The International Monetary Fund (IMF) draft Guide on Resource Revenue Transparency (December 2004) defines countries that are rich in hydrocarbons and/or mineral resources on the basis of the following criteria:
(i) an average share of hydrocarbon and/or mineral fiscal revenues in total fiscal revenue of at least 25% during the previous three years; or (ii) an average share of hydrocarbon and/or mineral export proceeds in total export proceeds of at least 25% during the previous three years.

Management of natural resource wealth in the short and long term is particularly difficult and therefore strong governance is needed. Factors that contribute to these difficulties include:

- price fluctuations in the commodity markets;
- the finite nature of resources;
- the unusually large size of the EI revenues in relation to national income;
- volatile transaction flows;
- the high cost and uncertain nature of exploration;
- a long gestation period before profits are realised;
- differing resource quality;
- differing taxation regimes;
- differing legal entitlements;
- country specific risk.

[1&2] The Extractive Industries (EI), for the purpose of this review, are defined as the Oil, Gas and Mining industries.

If these difficulties are not managed appropriately, they can contribute to poor economic performance and eventual dissipation of natural resource wealth. This occurs because hidden revenue flows provide ample scope for inefficient policies and corruption. There is a risk of diversion, misuse and misappropriation of revenues that can lead to a perception of insufficient benefits by local communities. This can become problematic, especially in high-impact projects where revenues are substantial in relation to the nation's fiscal income. Therefore, how countries distribute and manage revenues from EI is key. Revenue distribution and management in EI projects have also emerged as major factors for reputational and operational risks for investors. The risks involved are a deterrent to foreign investors.

The extent of this problem is wide and is not confined to Africa. Revenues from oil, mining and gas are critically important in about 60 developing or economic transition countries. Of the 3.5bn citizens in these countries, some 1.5bn live on less that US$2 per day. The World Bank identifies twelve of the world's most mineral-dependent states and six of the most oil-dependent states as Highly Indebted Poor Countries with among the worst Human Development Indicators in the world.

By improving transparency, it is hoped that natural resource wealth – a cause of corruption and authoritarianism in many countries – can become key in the fight against these problems.

"When a government is the direct beneficiary of a centrally controlled major revenue stream and is therefore not reliant on domestic taxation or a diversified economy to function, those who rule the state have unique opportunities for self-enrichment and corruption, particularly if there is no transparency in the management of revenues."

Some Transparency, No Accountability:
The Use of Oil Revenue in Angola and Its Impact on Human Rights, Human Rights Watch, January 2004

The benefits of increasing transparency

- **Improved investment climate**
  Political instability caused by opaque governance is a clear threat to investments. The operating companies are investing large amounts of resources and need to be assured of a stable, reliable environment for their investments. Companies stand to benefit from a more level playing field, a more predictable business environment and better prospects for security of their investments. Financial donors, international fiscal institutionals and other investors are more willing to offer finance and technical assistance to countries committed to, and implementing, transparent public financial management. And for investors, greater transparency should minimise risks arising from social and political instability, and ensure that they are able to exercise proper scrutiny over investment decisions.

- **Governments become more accountable**
  Transparency can make governments more accountable for their actions by enabling civilians to see how much companies are contributing to the national economy. Attention can then focus on the use of revenues by local, regional and national governments. Greater transparency about budgets and revenues will also go a long way to limiting opportunities for corrupt practices. Where there is a strong suspicion that government officials are acting in a corrupt manner, transparency can help prove or disprove allegations. It makes it more likely that existing resources and capacity will be better used and more difficult to divert money into corrupt pockets.

- **Improved living standards**
  One of the main drivers of conflict and insecurity is a lack of essential services and social and physical infrastructure. Ensuring that revenues from natural resources make it into government budgets for public sector expenditure (for example on health, education, access to drinking water) is key to reducing poverty and reducing the risk of conflict. This could lead to better social conditions and an improvement in living standards.

- **Reputational benefits for companies**
  For state-owned companies, transparency could provide reputational benefits domestically, in terms of demonstrating good corporate governance, openness and social responsibility. The companies would enhance their capital market access and their ability to attract partners in development. There are benefits to other stakeholders too. Industry bodies usually want their member companies to uphold the highest standards of transparency. Likewise, countries with companies that have large foreign interests want 'their' companies to be of good reputation by practising transparency in business transactions and operating in politically stable countries. These home countries are, in many cases, energy importers looking for more secure and stable sources of supply for the future.

- **Standards are set**
  Significant progress in improving transparency has already been made. The international community supports these efforts. The G8 countries issued a *Declaration on Fighting Corruption and Improving Transparency* at Evian in 2003. In 2004, *Transparency Compacts* were agreed with four countries. The International Monetary Fund (IMF) promoted fiscal transparency in member countries via the *Code of Good Practices on Fiscal Transparency* and the associated manual. Implementation of the code is monitored through the production of *Reports on the Observance of Standards and Codes* (ROSCs). Both the IMF and the World Bank promote more effective resource revenue management through policy advice, policy-based lending, project lending and technical assistance. More recently, the Extractive Industries Transparency Initiative has entered its implementation phase.

"Transparency over payments and revenues increases accountability and therefore the likelihood that the revenues generated by the development of natural resources are used in an efficient and equitable manner. It can also reduce the risk of diversions and misappropriation of revenues."

www.eitransparency.org
Official website of the Extractive Industries Transparency Initiative

The Extractive Industries Transparency Initiative

The EITI is a voluntary initiative, launched at the World Summit on Sustainable Development, in Johannesburg, September 2002. The aim of the initiative is to encourage greater transparency and accountability in countries dependent on revenues from oil, gas and mining. The intended outcome is to mitigate potential negative impacts of mismanaged revenues, thereby enabling these revenues to become an important engine for long-term economic growth that contributes to sustainable development and poverty reduction. The EITI begins a process whereby citizens can hold their governments to account for the use of those revenues.

Institutional investors have actively supported the initiative since it was developed. Newton, alongside a group of investors representing £3.8 trillion of funds under management, issued a statement of support for the initiative.

The initiative requires all Oil, Gas and Mining companies to publicly disclose all payments they make to developing country governments and for governments to publish what they receive. Published information is audited independently. It is participative in nature and encourages governments, extractive industry companies, international agencies and Non Governmental Organisations (NGOs) to work together to develop a framework to promote transparency of payments in the EI. There is a clear role for civil society, which participates actively in the design, implementation and overview of the disclosure process. The objective of such wide participation is to create a country-owned process.

The initiative has made good progress since its launch in 2002, though implementation is still at an early stage with only Azerbaijan and the Kyrgyz Republic having actually published numbers. Eleven countries have now committed to implementing the initiative. This includes three new commitments made this quarter from the Governments of the Republic of Congo, Niger and Cameroon. Other governments that have made a commitment to the EITI include Timor Leste, Ghana, Nigeria, Peru, São Tomé & Príncipe and Trinidad & Tobago.

During the first quarter of 2005, Azerbaijan published the first audited EITI report. This showed that payments received by the government amounted to roughly the same figure as that paid by the extractive industry companies. The small inconsistencies were explained.

So far, the experience of the initiative has shown that different countries take different approaches to implementation, leading to a criticism that the EITI lacks clear implementation guidelines and also a way to measure performance. These concerns were addressed at an EITI conference held in London on March 17th 2005. At the meeting, a set of EITI Criteria for all countries wishing to implement the EITI were mutually agreed. The voluntary nature of the initiative and country-specific implementation were highlighted as important foundations of the EITI.

Map of the world showing where the countries that are participants of the EITI are located.

The EITI Principles and Criteria are the core of EITI implementation for all participating countries. The Principles were agreed by a diverse group of countries, companies and civil society organisations at a conference in London in 2003. The Criteria were endorsed by participants of the EITI at the London Conference in March this year.

The EITI Principles

1. We share a belief that the prudent use of natural resource wealth should be an important engine for sustainable economic growth that contributes to sustainable development and poverty reduction, but if not managed properly, can create negative economic and social impacts.
2. We affirm that management of natural resource wealth for the benefit of a country's citizens is in the domain of sovereign governments to be exercised in the interests of their national development.
3. We recognise that the benefits of resource extraction occur as revenue streams over many years and can be highly price dependent.
4. We recognise that a public understanding of government revenues and expenditure over time could help public debate and inform choice of appropriate and realistic options for sustainable development.
5. We underline the importance of transparency by governments and companies in the extractive industries and the need to enhance public financial management and accountability.
6. We recognise that achievement of greater transparency must be set in the context of respect for contracts and laws.
7. We recognise the enhanced environment for domestic and foreign direct investment that financial transparency may bring.
8. We believe in the principle and practice of accountability by government to all citizens for the stewardship of revenue streams and public expenditure.
9. We are committed to encouraging high standards of transparency and accountability in public life, government operations and in business.
10. We believe that a broadly consistent and workable approach to the disclosure of payments and revenues is required, which is simple to undertake and to use.
11. We believe that payments' disclosure in a given country should involve all extractive industry companies operating in that country.
12. In seeking solutions, we believe that all stakeholders have important and relevant contributions to make – including governments and their agencies, extractive industry companies, service companies, multilateral organisations, financial organisations, investors, and non-governmental organisations.

The EITI Criteria

1. Regular publication of all material oil, gas and mining payments by companies to governments ("payments") and all material revenues received by governments from oil, gas and mining companies ("revenues") to a wide audience in a publicly accessible, comprehensive and comprehensible manner.
2. Where such audits do not already exist, payments and revenues are the subject of a credible, independent audit, applying international auditing standards.
3. Payments and revenues are reconciled by a credible, independent administrator, applying international auditing standards and with publication of the administrator's opinion regarding that reconciliation including discrepancies, should any be identified.
4. This approach is extended to all companies including state-owned enterprises.
5. Civil society is actively engaged as a participant in the design, monitoring and evaluation of this process and contributes towards public debate.
6. A public, financially sustainable work plan for all the above is developed by the host government, with assistance from the international financial institutions where required, including measurable targets, a timetable for implementation, and an assessment of potential capacity constraints.

Engagement with Companies in the Extractive Industries

With the quarterly focus on the Extractive Industries and the EITI, we decided, for this report, to make contact with some of the companies held by Newton's clients. This was to ascertain their level of participation in and the progress being made by the EITI. We contacted the following companies:

Shell, Total, Xstrata, BP, Repsol, BHP Billiton and Anglo American.

The over-riding outcome of the responses was that the companies were very positive with regards to the EITI and what it is trying to achieve. Business is about the long-term and, therefore, EI companies have a direct interest in the health and stability of the areas in which they operate. Some companies were more open in supporting the initiative than others. However, this was usually because they were active in more countries that had adopted the initiative than others. One company had taken a "wait and see" approach during the pilot phase of the initiative, but stated it fully supported the drivers behind it. Notably, all the companies were willing to co-operate with whatever lead governments take and stated a positive attitude of working openly with governments on improving transparency.

What a company's responsibility is towards influencing a government is an interesting debate. BP learned the hard way that individually pushing for a positive change in a corrupt country can compromise commercial interests. Before the EITI was developed, when other campaigns to increase transparency were gaining momentum, EI companies were encouraged to use their influence to push for reform. In the case of Angola, when BP took individual action to try to improve transparency, the outcome was not encouraging.

BP's experience highlights the need for the powerful participative nature of the EITI. It also highlights that there is a large role for individual populations of a country to take in holding their government accountable for the use of revenue derived from resource extraction.

The main challenge of the EITI was found to be the need to be adaptable as each country is a special case. Each country has a different civil society, a different set of issues to overcome, as well as different levels of transparency. Therefore, implementation for every country must be specific.

Case Study: BP's Experience in Angola

In 2001, BP announced that it would henceforth reveal its payments to oil-country governments worldwide. It implemented its new policy in a US regulatory filing. For the rights to operate an offshore well, BP said it had paid Angola a signature bonus[3] of US$111 million. BP's Initiative was widely reported in the international press. Angolan officials reacted harshly. "It was with great surprise, and some disbelief, that we found out through the press that your company has been disclosing information about oil-related activities in Angola, some of which have a strictly confidential character," Manuel Vicente, head of state-owned oil group Sonangol, said to BP in a letter copied to the other oil companies operating in Angola – "Given the seriousness of the situation", he warned, "if the provision of information by your company is confirmed and we observe moral or material damage thereof, we reserve the right to take appropriate action". He threatened BP with "contract termination".

[3]A signature bonus is cash paid upfront upon signing a contract. For Angolan offshore drilling rights, the signature bonuses have typically been around the US$100 million to US$400 million per block. Anywhere in the world, it is standard practice for oil companies to pay signature bonuses. In an auction of anything, there are good reasons for the seller to ask for an upfront payment in addition to royalties. The use of signature bonuses is not a sign of corruption; it is sound auction design. However, there are two considerations to be wary of: the size of the signature bonus relative to the royalty rate and where the money ends up.

Country Focus: Nigeria

Africa is at the heart of several global development initiatives during 2005. The main ones include:

- **Replenishing of resources for the International Development Association (IDA – the World Bank's lending arm to developing countries.)**
  On February 22, 2005, donor countries reached agreement on a substantial replenishment of funds to the IDA. At least $34 billion in resources will be made available during the next three years, specifically for development assistance. This represents, at a minimum, a 25 percent increase in overall resources over the previous replenishment. This is the largest expansion of IDA resources in two decades.

- **UK Commission for Africa**
  The Commission was formed last year with the task of defining the challenges facing Africa and to provide clear recommendations on how to support the changes needed to reduce poverty. A report was produced on March 11th, titled "Our Common Interest".

- **The G8 Summit**
  The UK takes the presidency this year. The summit is being held in July at Gleneagles in Scotland. One of the major focuses is 'The Challenge of Africa'.

- **The progress report by the United Nations on efforts to achieve the Millennium Development Goals (MDGs)**
  In 2000, the international community set itself eight goals to achieve by 2015. The MDGs include targets on eradicating extreme poverty, combating HIV/AIDS and malaria, and ensuring that every child receives primary education. The UN Millennium Review Summit in 2005 will consider progress towards the MDGs. Much more needs to be done in Sub-Saharan Africa if the MDGs are to be met. This is one of the reasons why UK Prime Minister, Tony Blair, has said that Africa will be a priority of the G8 Summit in Gleneagles. It is also one of the reasons why the Prime Minister set up the Commission for Africa.

- **The World Bank's Global Monitoring Report**
  This Report provides an integrated assessment of the policies and actions needed to achieve the Millennium Development Goals.

With such a focus on Africa, it is relevant to do a specific country focus. Nigeria was chosen due to the exposure Newton's clients have to this country through their investment in Shell Transport & Trading Plc.

Nigeria: A Snapshot Profile

Country overview

President: Olusegun Obasanjo (since May 29, 1999)

Vice President: Atiku Abubakar

Independence: October 1, 1960 (from United Kingdom)

Population (2004E): 137.3 million

Location/Size: West Africa, bordering the Atlantic Ocean (on the south and west), Cameroon (on the south), Chad (on the east), Benin (on the west) and Niger (on the north)

Religion (2004E): Islam (50%), Christianity (40%), traditional beliefs (10%)

Number of States: 36 and 250 different ethnic groups

Capital: Abuja

Area: 923,768 sq km (356,669 sq miles)

Life expectancy: 51 years (men), 52 years (women) (UN)

Economic overview

Finance Minister: Ngozi Okonjo-Iweala

Currency: Naira

Market Exchange Rate (31/03/05): US$1 = 133.0 Naira

Gross Domestic Product (2003E): $48.4 billion **(2004F):** $53.2 billion

Real GDP Growth Rate (2002E): 3.5% **(2003E):** 4.2% **(2004F):** 4.4%

Inflation Rate (2002E): 12.9% **(2003E):** 14% **(2004F):** 16.9%

Current Account Balance: (2003E): $2.0 billion **(2004F):** $3.5 billion

Major Trading Partners: United States, France, India, United Kingdom, Spain, Germany, Brazil

Major Export Products: Crude oil, natural gas, cocoa, rubber, timber, manufactured goods

Major Import Products: Petroleum products, food, machinery and equipment, manufactured goods

Oil Export Revenues (2003E): $20.9 billion (2004F): $27.0 billion

Oil Export Revenues/Total Export Revenues (2003E): 96%

Total External Debt (2003E): $30.2 billion

Source: Energy Information Administration, Country Analysis Brief (August 2004): Nigeria

Background to the conflict and tension in Nigeria
Nigeria is the largest oil producer in Africa and the fifth-largest oil producer within OPEC. Nigeria is strategically important on a global basis due to the abundance of oil and gas reserves, the ease of accessibility to these reserves and the high quality/low sulphur content of oil produced in the region.

Nigeria's economy is overwhelmingly dependent on the production of crude oil. Oil exports account for 96% of Nigeria's total exports. Political and ethnic strife has been disrupting oil production in Nigeria for nearly fifty years and disputes between oil companies, the government, and communities are common. Despite the wealth generated by the extraction of oil, currently seven out of ten Nigerians live on less than US$1 per day, which is widely accepted as the measure of absolute poverty in Africa by the World Bank.

The Nigerian State, even with the availability of resources and the wealth that is generated through oil production, is widely perceived to lack the necessary governance to ensure a minimum core level of economic, social, and cultural rights. The lack of these is one of the main drivers of conflict and insecurity in the region.

Other issues contributing to the conflict include:
- ethnic rivalry;
- the disproportionate allocation of economic resources between communities;
- high unemployment in the region;
- measures taken by companies to protect assets (fixed assets of oil companies, such as installations and pipelines); and
- the use of force by criminals involved in illegal oil bunkering (theft of crude oil).

Due to the overwhelming presence in the region, oil companies are often viewed, alongside government officials, as exploiting the region and its resources. As a result, the companies often become the targets of sabotage and violence.

As institutional investors, we are mindful of the risks and responsibilities that our investee companies face when they operate or have business relationships in troubled countries, such as Nigeria. As outlined above, operating in this type of environment exposes companies to heightened business risks. Foreign direct and indirect investment provided by companies operating in the area can be influential in positive ways, for example through community development, as well as in negative ways, such as sustaining a corrupt regime. As a significant shareholder, on behalf of our clients, in Shell Transport & Trading Plc, we thought it useful to meet with the company's management to gain a better understanding and to seek assurance that the risks associated with operating in Nigeria are fully recognised and considered.

Company Focus: Shell

Shell operates in a very sensitive operating environment in Nigeria. The largest oil joint venture in Nigeria is operated by Shell and produces nearly 50% of Nigeria's crude oil. Corruption and the theft of crude oil (illegal oil bunkering) are two major problems faced by the company. Nigeria accounts for c.10% of Shell's worldwide production and remains critical to the group in its attempts to restore its fortunes after the 4.47bn barrel write-down in proven reserves last year.

Shell has been operating in Nigeria for nearly 60 years. Shell has the largest network of land-based assets in Nigeria and employs nearly 4,000 people directly with another 10,000 on contract. It owns some 87 flow stations, eight gas plants, c. 1,000 wells, and runs a network of pipelines through the Niger Delta, which stretches along 6,000 kilometres. Of the other companies operating in Nigeria, Chevron-Texaco and Nigeria Agip Oil Company (NAOC) have some exposure to the onshore Delta itself; the operations of Exxon-Mobil, Total and Statoil are primarily offshore. Note that offshore operations are less vulnerable to sabotage and illegal oil bunkering.

Newton requested a meeting with Shell to discuss the risks involved in operating in Nigeria. We were seeking assurance from the group that:

1) the risks of operating in such a challenging environment were fully recognised;
2) effective policies, procedures and systems were in place for managing the risks associated with operating in Nigeria, and;
3) appropriate engagement with the government and local communities concerning the various issues and risks was taking place.

The meeting also gave the opportunity to discuss political risk, operating and environmental risk, and security and transparency issues. In February 2005, Newton met with four representatives from Shell.

Findings and Conclusions
Shell faces significant challenges in Nigeria but has considerable experience in dealing with them. The company is aware of and understands the risks associated with operating in Nigeria. It also understands that it has a role to play in contributing towards the sustainable development of society and that it can influence and encourage positive change. The business opportunities currently outweigh the associated risks for a company that has a long-term vision and solid business practices.

- **Reform and the fight against organised crime**
  The meeting highlighted that illegal oil bunkering and the problems associated with organised crime are the main cause of social unrest and instability in the Nigeria. Shell believes that organised crime is now at an unsustainable level. The company is taking a proactive approach to ensure the government is aware of the extent of the problem by reporting the estimated amount of oil that is lost due to theft on a weekly basis. President Obasanjo's reform agenda will slowly improve the climate for business in Nigeria. However, in the near-term, risks are greater than ever as the beneficiaries of corruption and crime attempt to maintain their "thiefdoms". More encouragingly, Shell commented that, excluding conflict related to the theft of crude oil, it could be argued that conflict in Nigeria is diminishing.

- **Lack of transparency on the spending of oil revenues by the government**
  There is growing evidence that awareness by civilians of unexplained discrepancies in oil earnings reported to be returned to the community, and what is actually spent in terms of community development, is emerging. Recently there have been indications that civil society is beginning to see that the government (at a local level) needs to be more transparent on the spending of oil revenues. The government is taking a strong stance in trying to improve transparency as evidenced by the commitment made by President Olusegun Obasanjo to the EITI in November 2003. The EITI was launched in Nigeria in February 2004. Shell has set an example for other oil companies in Nigeria by being the first and only company to publish details of payments made to the government in terms of royalties, taxes, signature bonuses etc.

- **Operational issues**
  The main operating issue recently faced by the company was the downgrade of reserves experienced last year. Since then Shell will only book reserves under the strict interpretation of the SEC rules, which the company has adopted. This in turn appears to have led to a review of project priorities, with Shell more inclined to spend incremental capital on offshore projects which are less vulnerable to sabotage. Shell pointed out that it really has three businesses in the Nigerian upstream: onshore oil production, offshore oil production and the gas and LNG business. This allows for diversification away from vulnerable operations if required. The group is being careful not to overcapitalise the more vulnerable business locations. Shell has also adopted global procedures for implementing maintenance and inspection programmes. Prior to 2000, these had been done on an ad-hoc basis. Since 2001 and the adoption of these new procedures, pipeline operational incidents have been significantly reduced.

- **Political issues**

  Shell has faced numerous political issues over the years it has been operating in Nigeria. The group has always maintained that it has worked within the governing laws of Nigeria. It is not unreasonable to expect a large multi-national company to work to standards above and beyond a host country's governing laws – especially if the local laws are lacking in strength. Shell believes it has made a sustained effort to help build a stable, functional and peaceful community. This does, after all, help to improve the operating and business environment.

  Shell continues to face Class Action Law Suits. Currently there is one outstanding, a combination of 2 different claims. The first claim was filed in 1996 by relatives of the nine people executed for a fatal attack on former leaders of the Movement for the Survival of Ogoni People (Mosop). The case was widely reported to be a legal farce. The defendants were found guilty of murder by military tribunal and executed in November 1995. The Class Action alleges that Royal Dutch Petroleum and Shell Transport & Trading ordered the government to carry out the executions or alternatively that they conspired with the government with regard to the executions. Shell vehemently denies this. From the company's perspective, there is no evidence to substantiate this claim.

  The second part of the class action was filed in 2002 and is for alleged human rights abuses in Ogoniland. The class action is yet to be certified and is in the discovery and deposition stage. Shell again vigorously denies these allegations and believes them to be unsubstantiated.

  There is also a Resolution from the House of Representatives and Senate Committee of the Niger Delta. The resolution requires Shell to pay $1.5bn to the Ijaw Aborigines of Bayelsa State as "compensation for severe health hazard, economic hardship, injurious affection, avoidable deaths and sundry maladies suffered as a direct or indirect consequence of multiple spillages occurring in SPDC's[4] facilities". Shell is refusing to pay as the group believes the claims to have no legal or scientific basis. The DoPR[5] and the Nigerian Federal Government have indicated they are in agreement with Shell.

- **Community development**

  Shell over the years of operation in Nigeria has continued to evolve its community development and assistance contributions. 2004 saw the implementation of the Sustainable Community Development (SCD) Strategy with the objective of improving the quality of life and maintaining mutually beneficial relationships with communities in the Niger Delta. In addition, a thematic approach was adopted focusing primarily on the key areas of economic empowerment, human capital development, healthy living and basic services. The SCD strategy places greater emphasis on partnerships, not just with the communities, but also with Government and strategic local and international development organisations and NGOs.

[4] SPDC = Shell Production Development Company (Nigeria)
[5] DoPR = Department of Petroleum Reserves

Examples of engagement – SRI

Please note that this activity log shows examples of SRI engagement over the quarter. It is not an exhaustive list of all engagement. A complete list of how Newton voted on securities during the period is available upon request.

- **Disclosure monitoring**
  In March, Newton adopted a more formal approach to the monitoring and recording of disclosure levels on social, ethical and environmental reporting for UK holdings. It is now Newton's policy to vote against the adoption of the Report and Accounts, should disclosure in social, ethical and environmental issues fail to reach acceptable standards.

- **Shell Transport & Trading Plc**
  Company meeting – February 2005
  Meeting discussed in the company focus section of this report.

- **Croda**
  Company Meeting – February 2005
  Croda executives came into Newton for a meeting. Part of the discussion involved details of a £5m environmental liability to cover remedial costs to a site being disposed of as part of the group's portfolio reorganisation. The site was in need of decommissioning. For the decommissioning, Croda designed a novel clean-up process, for which they received approval from government inspectors. It was encouraging to see Croda put such investment into decontamination and dismantling of retired, contaminated facilities and removal and/or disposal of the resulting wastes.

- **Nestle**
  SRI Conference: Nestle Commitment to Africa – March 2005
  An overview of the company's exposure to Africa, including the pressures of operating responsibly in such a diverse environment, was given. Social and economic impacts of the company's actions were highlighted. An outline of the impacts of the company's policy of direct dealings with local businesses (such as local farmers) was also given. Through dealing directly with local businesses, the group endeavours to create a sustainable cycle through the value chain. Nestle's initiatives and work on combating issues such as HIV/AIDS and poverty were highlighted. Nestle also stated that marketing for powdered milk is only directed at doctors. It is therefore a decision for a doctor whether to prescribe powdered milk to a patient. Nestle works within the guidelines of the World Health Organisation as well as within it's own strict internal policies for the sale of powdered milk. The presentation successfully showed that Nestle is committed to long-term sustainable business development in Africa. The group believes there are business opportunities for those able to have a long-term vision and solid business practices.

Ian Burger – Associate Director of Investment Management, Corporate Governance Officer
Katie Swanston – SRI Officer

Company Meeting Log

During the quarter, Newton analysts and fund managers had individual meetings with the management of 247 companies to initiate or maintain dialogue around financial performance and/or responsible investment matters. The insights gained through this engagement are used when making investment decisions. Meetings were held with the following companies:

Absa
Acambis (x 2)
Acciona
Accor
Acom
Adamind
Advanced Info Services
Advanced Medical Solutions
Aero Inventory
Aggreko
Aiful
Air Liquide
All America Latina Logistica
Alliance Unichem
Alpha Airports
Altadis
Altair Nanotechnology
Alternative Networks
AMB Generali
Amec
Amlin
Anadarko
Anite
Applied Optical Technologies
Aquarius Platinum
ARK Therapeutics
Asia Energy
Associated British Ports
Astrazeneca
Astro All Asia Networks
Axalto
BAE Systems (x 2)
Banca Populare di Verona
Bank of Yokohama
Barclays
BBA Group
Beckman Coulter Inc
Belgacom
Bespak
BG Group
BHP Billiton
Blockshield
BPP
Brambles
Britannic Group
British American Tobacco
British Energy
British Sky Broadcasting
Brixton Estates
Bunzl
Bursa Malaysia
Cadbury Schweppes
Cairn Energy
Capita Group
Carlsberg
Carter & Carter
Catlin Group
CCR Logistics
Centrica
Chiba Bank
Chrysalis
City North
Cobham
Coca-Cola Co
ConocoPhillips
Creston
CRH
Croda International
CSL Limited
Daiwa
Datamonitor (x 2)
Davis Service Group
DBS
Derwent Valley
Deutsche Boerse
Deutsche Postbank
Dis Deutscher Industrie Service
Dixons
Domino Printing
eAccess
Electrabel
Elior
Elisa Corp
Emblaze
Encana
Erste Bank
Essilor International
Exel
Fastweb
Fraport
Frontera
Gallaher
Geophysique
GFI
GKN
GlaxoSmithKline
Go-Ahead Group
Goldshield
Halma
Hanson
Helphire
Hitachi Chemical
Hitachi Ltd
Holcim
Homeserve
Huntleigh
Hutch Telecom
HypoVereinsBank
ICM
IFX
Incisive Media
Inovio
Intercell
Interlink
International Power
Interserve
Intertek
Intesa
Irish Life & Permanent
ITV
Joyo Bank
Jupiter Telecom
KBC
Kikkoman
Kimberley Diamond
Kirby Corp
Kone
KT Corp
Lafarge
Land Securities
LG Electronics
Liontrust
Logitech International
MAN AG
McKesson
Medical Property
Meitec
MFI Furniture
Minerva
Misys
Mitsubishi Tokyo Financial
Mizuho Financial
Monex Beans
Monsanto
National Express
National Grid Transco
Natura Cosmeticos
NCC
NEC Electronics
Newport Networks
Nipson Digital Printing
Noble Group
Nokia
Nomura
Nord Anglia
Norsk Hydro
Northern Rock
Ocean Power Technologies
Olam International
Oncolytics Biotech
Pantheon Investment Trust
Parkway Holdings
Partner Communications
Petrochina
Plasmon
Polaron
Porvair
Premier Foods
Primary Health Properties
Procter & Gamble
Promise
Provident Financial
Prudential
Publicis Groupe
Quadnetics
RAC
Rank
Rational
Raymarine
Redbus
Repsol
Reuters
Rexam
Rio Tinto
Robert Walters
Royal & Sun Alliance Insurance Group
Royal Bank of Scotland
RWS
Safeway
Samsung Electronics
Sanpaolo Imi
Sarantel
Scottish & Newcastle
Scottish & Southern Energy
Scottish Power
Serco
Shed Productions
Shell Transport & Trading (x 2)
Shinsei Bank
SHL
Shuffle Master
Siam Cement
Singapore Exchanges
Singapore Telecom
sit-up.com
Smith & Nephew
Societe Generale
SolarWorld
Square Enix
St Modwen
Statoil
Stolt Offshore
Stora Enso
Straumann
Sumitomo Mitsui
Syngenta Healthcare
TDK
Television Francaise
Tomkins
Total
Toyota
TurboChef Technology
UFJ
Ultimate Leisure
Ultra
Unicredito
Unilever
United Healthcare
Verbund
Weir Group
West Japan Railway
Westpac
Whitbread
Wilson Bowden
Wolters Kluwer
Wolverhampton & Dudley Breweries
Wood (John) Group
Woodside
Workspace Group
WPP Group
WW Grainger
Xstrata
Zurich Financial Services

In addition, the analysts and fund managers attended a large variety of external meetings arranged by companies, brokers and other research providers.

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Issued and approved by Newton Investment Management Limited,
Mellon Financial Centre, 160 Queen Victoria Street, London EC4V 4LA.

Registered in England No. 1371973.

Authorised and regulated by the Financial Services Authority

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The Bank of New York Mellon Centre
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13330R 03/09